RE: Rule 2-200
8/27-28/04 Commission Meeting
Open Session Item III.C
Supplemental Mailing

Memorandum

To: Rules Revision Commission

From: Stanley W. Lamport

Date: August 10, 2004

Re: Rule 2-200 - Law Firm Definition

As the Commission will recall, an open issue with respect to the draft revision to rule 2-200 concerns the definition of "law firm." The following is my suggested definition, which consists of two parts, a law firm definition and a definition of when a lawyer is part of a law firm.

A. Law Firm Defined

"Law firm" means an association of two or more lawyers practicing law together, including

(A) An association whose activities constitute the practice of law consisting of two or more lawyers who share profits, expenses and liabilities, including a partnership, corporation and limited liability partnership or company.

(B) A sole proprietorship or professional corporation whose activities constitute the practice of law that employs more than one lawyer.

(C) A division, department, office, or group within a business or governmental entity whose activities constitute the practice of law that consists of more than one lawyer.

(D) A publicly funded entity whose activities constitute the practice of law that consists of more than one lawyer.

B. Lawyer As Part of a Law Firm

A lawyer is part of a law firm if the lawyer has an ownership interest in the law firm or has a close, personal, continuous and regular relationship with the law firm.

C. Thoughts and Comments

My criticism of the law firm definitions that have been swirling around so far is that they do not have an entity focus. A law firm is an entity (whether incorporated or unincorporated). The definition should focus on the entity, which I try to do in this draft.

I have tried to keep the law firm definition broad and flexible, which is why I used the term "association." Our current definition in rule 1-100 focuses more on types of entities, which is not as inclusive as the definition I am proposing. An added concern is that we not adopt a definition that is "culture bound" in the sense of assuming the kinds of entities that are common today and not leaving room for new kinds of entities to arise in the future. The "association" terminology addresses that concern.

At the same time, I have narrowed the focus of the definition to associations to practice law, which would exclude from the definition associations between lawyers to perform non-legal services.

The definition is also limited to the concept of an association of two or more lawyers. It excludes associations between a lawyer and non-lawyers to provide legal services, which is prohibited under other rules.

The lawyer as part of a law firm rule relies heavily on the terminology in Standard 8 in rule 1-400. Rather than focusing on whether there is an employment relationship, which plagues our current definition of associate, I have picked up the close, personal, continuous and regular language to characterize the relationship. A lawyer does not have to meet an employment test to be part of a law firm, but the lawyer has to have a close enough relationship to meet the client expectation that the lawyer is part of the firm, which the Standard 8 language seeks to achieve.

I considered limiting the lawyer in firm definition to lawyers who regularly and continuously practice law under the name of the law firm, but ultimately rejected the concept. The lawyer in the firm definition I have drafted is broader. It includes lawyers who are not practicing law under the name of the firm, but otherwise meet the elements of the relationship test. This would include retired or non-equity partners who do not have an ownership interest and, in the case of the former at least, may not be practicing law with the firm. This approach also embraces some conflict of interest concepts, which I think are already the law since at least *SpeeDee Oil*.

Assuming we go with something along the lines of this definition, I would revise the discussion to rule 2-200 to replace "outside lawyer" with "a lawyer who is not part of the member's law firm," which would address the comment from Becky Stretch.

Memorandum

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From: Stanley W. Lamport

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Re: Rule 2-200 – Should There Be A Rule?

In looking over the comments to the draft rule, it seems to me that before we reach a consensus on the comments we need to consider a threshold question – should there be a rule? If there should be a rule, why should there be a rule? I realize that an author who toils on a rule can become invested in its existence – probably because nature abhors a waste of energy. However, I am prepared shed my assigned bias to initiate this discussion.

I am told that a definition of insanity is doing the same thing over and over and expecting a different result. Given the consistent results in *Kallen v. Delug, Scolinos v.Kolts*, *Margolin v. Shemaria*, and *Chambers v. Kay*, one could surmise that such a form of insanity is gripping an uncomfortably large segment of our profession. If we assume that the lawyers in these cases are not insane, we are left with the possibilities that either they are not reading the rule or they do not understand the rule. In either case, it appears that the rule is running counter to what many lawyers consider an accepted (or at least an acceptable) practice.

It appears from some of the comments there is concern that the rule is allowing some lawyers to accept referrals by representing they will pay a referral fee and then later violating that promise with impunity. There also seems to be a concern about the State Bar actually prosecuting lawyers who enter into agreements to divide fees without complying with the rule, as apparently occurred with the lawyers in *Chambers*.

So why have a rule? If the purpose of the rules includes protecting clients and promoting trust and confidence in the legal profession (without attempting to debate another agenda item), does the rule serve any such purpose?

The rule itself suggests two rationale: 1) that the total fee should not increase solely by reason of the division, and 2) that the total fee charged should not be unconscionable. However, neither rationale seems to be a compelling reason for the rule. A member can never charge an unconscionable fee. We do not need a separate rule to do what rule 4-200 already is supposed to do. Furthermore, if the fee is not unconscionable and the client consents, why would we nevertheless prohibit an increased fee due solely to the division? In other words, if my regular hourly fee is $150.00 (truly a hypothetical) and I increase my fee to $250.00 solely because of the agreement to pay a referral fee, why should we prohibit the $250.00 fee if the client is fully informed and consents?

Another rationale for the rule comes from LACBA Formal Opinion 467, which looked at three factors: 1) whether the client is actually retaining the best lawyer for the work or whether the member's involvement is based on the member's agreement to divide the fee; 2) whether the member dividing the fee will devote sufficient time to the matter in light of the fact that the member will be receiving a reduced fee; and 3) whether the client may prefer to negotiate a more favorable arrangement directly with the member.

The first of these two factors would advance trust and confidence in the legal profession and protect clients by fostering disclosure of the basis of a referral and allowing the client to be aware of and question whether the lawyer to whom the matter is referred is appropriate and will diligently represent the client's interests. The third factor relates to the client's freedom of contract that allows the client to address the lack of diligence concern by negotiating something different. Of course the rule also gives the client the power to nix the deal by not consenting; but the only way to avoid that situation is to allow lawyers to divide fees without ever disclosing the division to the clients, which would be acceptable only if there is no reason to have a rule at all.

Do these policies justify having a rule? Do the litigation and disciplinary consequences to lawyers outweigh the benefit to clients and the public of having a rule?